

# Report of the auditor-general to the Eastern Cape Provincial Legislature and Council

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Makana Local Municipality as set out on pages ... to ..., which comprise statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Makana Local Municipality as at 30 June 2017, and financial performance and cash flows for the year then ended in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

### Basis for qualified opinion

#### Irregular expenditure

3. The municipality did not have adequate systems to identify and disclose all irregular expenditure incurred during the year as required by section 125(2)(d)(i) of the MFMA. The irregular expenditure disclosed in note 41 to the financial statements is understated in respect of amounts incurred and identified during the audit process of R25, 5 million. Due to the lack of systems it was impracticable to determine the full extent of the understatement of the irregular expenditure disclosed as R4, 4 million (2016: R38, 3 million) in note 41 to the financial statements.

#### Receivables from exchange transactions

4. The municipality did not account for receivables from exchange transactions in accordance with the requirements of GRAP 104: *Financial instruments* and did not measure debtors when the measurement criteria had been met as debtors were not correctly valued and completely impaired. As a result, receivables from exchange transactions, as disclosed in the statement of financial position and note 3 to the financial statements, are overstated by R43, 0 million (2016: R35, 7 million) and accumulated surplus was overstated by R30,9 million and VAT by R10,2 million .
5. I was unable to obtain sufficient appropriate evidence for receivables from exchange transactions as there was inadequate supporting documentation for debtors with credit balances and the impairment of receivables from exchange transactions. I was unable to confirm receivables from exchange transactions by alternative means. Consequently, I

was unable to determine whether any adjustments to receivables from exchange transactions of R 46,1 million (2015-16: R35,8 million) as disclosed in the statement of financial position and as disclosed in note 3 to the financial statements were necessary.

#### Receivables from non-exchange transactions

6. I was unable to obtain sufficient appropriate evidence for receivables from non-exchange transactions as there was inadequate supporting documentation for debtors with credit balances and the impairment of receivables from non-exchange transaction. I was unable to confirm receivables from non-exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments to receivables from non-exchange transactions as disclosed in note 4 to the financial statements and stated at R 25, 7 million were necessary.
7. The municipality did not account for receivables from non-exchange transactions in accordance with the requirements of GRAP 104: *Financial instruments* and did not measure debtors when the measurement criteria were met. Debtors were not recorded at appropriate amounts and were not adequately impaired. As a result, receivables from non-exchange transactions, as disclosed in the statement of financial position and note 4 to the financial statements, are overstated by R12,9 million and accumulated surplus is overstated by the same amount.

#### Revenue from exchange transactions

8. The municipality did not measure revenue at the fair value of the consideration received or receivable in accordance with GRAP 9, *Revenue from exchange transactions*. This was due to management not having adequate systems to recognise revenue and ensure that it was correctly accounted and recorded. Consequently, revenue from exchange transactions disclosed in the statement of financial performance and note 18 is overstated by R41,9 million and receivables from exchange transactions as disclosed in the statement of financial position and note 3 to the financial statements is overstated by the same amount.
9. I was unable to obtain sufficient appropriate audit evidence for revenue from exchange transactions as other income transaction could not be substantiated by the supporting evidence provided for audit. I was unable to confirm the revenue transactions by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to revenue from exchange transactions stated at R9, 9 million in note 21 to the financial statements.

#### Value Added Tax (VAT) Payable

10. Sufficient appropriate audit evidence was not available to support the value added tax (VAT) payable disclosed in note 14 to the financial statements. The municipality does not have the adequate controls and system to maintain the transactions on the Vat suspense account was unable to obtain the required evidence by alternative means. Consequently, I was unable to determine whether any adjustments to VAT payable of R14, 3 million (2015-16: R5, 0 million) disclosed in note 14 to the financial statements were necessary.

## Unauthorised expenditure

11. I was unable to obtain sufficient appropriate audit evidence regarding the unauthorised expenditure as disclosed on note 39 to the financial statements, as the disclosure was presented in the financial statements for auditing purposes without accurate and complete underlying accounting records. I was unable to audit the disclosure in the financial statements by alternative means. Consequently, I was unable to determine whether any adjustments to the unauthorised expenditure of R356, 6 million as disclosed in note 39 to the financial statements was necessary.

## Cash flow statement

12. The presentation of the cash flow statement was not in accordance with GRAP 2: *Cash flow statements*. Cash flows from operating activities and cash flows from investing activities in the cash flow statement have been incorrectly presented. Consequently, the net decrease in cash and cash equivalents as disclosed on the cash flow statement is understated by R31, 0 million (2016: R159 million).

## Corresponding figures

### Employee related costs

13. I was unable to obtain sufficient appropriate evidence for employee related costs disclosed in the 2015-16 financial statements. During the current year, I was again not provided with information required to substantiate these transactions because the municipality did not have adequate systems to maintain records of employee related costs. I was unable to substantiate these transactions by alternative means. Consequently, I was unable to determine whether any adjustments to the corresponding figure for employee related costs of R161,1 million disclosed in the statement of financial performance and note 27 to the financial statements.

## Context for the opinion

14. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
15. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
16. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

## Material uncertainty related to financial sustainability

17. I draw attention to the matter below. My opinion is not modified in respect of this matter.

18. As disclosed in note 52 to the financial statements, the municipality is facing a number of financial risks that cast doubt on its ability to sustain its current level of operations in the near future. The key financial risks identified include:

- an inability to pay creditors within due dates
- negative key financial ratios including a net current liability position.
- In addition, the actions taken by management to mitigate the impact of these risks are disclosed in this note.

### **Emphasis of matters**

19. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Restatement of corresponding figures**

20. As disclosed in note 47 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2017.

### **Fruitless and Wasteful expenditure**

21. As disclosed in note 40 to the financial statements, fruitless and wasteful expenditure to the amount of R5, 5 million (2016: R9, 9 million) was incurred, as a result of interest paid on overdue accounts.

### **Significant uncertainties**

22. As disclosed in note 44 to the financial statements, the municipality was the defendant in a number of lawsuits estimated at R39, 9 million (2016: R43 million). The outcome of these lawsuits cannot be determined at present as litigation is still in progress.

### **Financial sustainability**

23. As disclosed in note 52 to the financial statements, the municipality is facing a number of financial risks that cast doubt on its ability to sustain its current level of operations in the near future. The key financial risks identified include:

- an inability to pay creditors within due dates
- negative key financial ratios including a net current liability position.

In addition, the actions taken by management to mitigate the impact of these risks are disclosed in this note.

### **Material Losses**

24. As disclosed in note 49 to the financial statements, material electricity losses to the amount of R94, 5 million (2016: R38,6 million) was incurred which represents 13% (2016: 60.7%) of total electricity purchased. Material losses were due to tampering of meters, faulty meters and illegal connections

## **Other matter**

25. I draw attention to the matter below. My opinion is not modified in respect of this matter.

### **Unaudited disclosure notes**

26. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

## **Responsibilities of accounting officer**

27. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with SA Standards of GRAP and the requirements of the MFMA and the DoRA and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

28. In preparing the financial statements, the accounting officer is responsible for assessing the Makana Local Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting officer either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

## **Auditor-general's responsibilities for the audit of the financial statements**

29. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

30. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

## **Report on the audit of the annual performance report**

### **Introduction and scope**

31. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.

32. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated

the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

33. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2017

<b>Development priorities</b>	<b>Pages in the annual performance report</b>
KPA 1 – Basic service delivery and infrastructure development	x – x
KPA 2 –Local economic development	x – x

34. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
35. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

## **KPA 1 Basic service delivery and infrastructure development**

### **Usefulness**

#### **Reported indicators and targets not consistent when compared with planned indicators and targets**

##### *Upgrading 3m of Kwa Nomzamo Internal Road at Riebeeck East*

The indicator was reported as Upgrading 3 m of KwaNomzamo Internal Road at Riebeeck East and the target was reported as 1 KM upgraded while the indicator and target was not included in the approved integrated development plan and service delivery and budget implementation plan. This is not in line with the requirements of section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (for municipalities).

##### *Approval of design and drawings for the Waainek Bulk Water Supply*

The indicator and target was reported as Approval of design and drawings for the Waainek Bulk Water Supply while the indicator and target was not included in the approved integrated development plan and service delivery and budget implementation plan. This is not in line with the requirements of section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (for municipalities).

**Performance indicators were not well-defined and targets were not specific, measurable and time bound**

**Various indicators**

36. I was unable to obtain sufficient appropriate evidence that clearly defined the predetermined source information and evidence and method of collection to be used when measuring the actual achievement for the various indicators, as required by the Framework for managing programme performance information (FMPPI). This was due to a lack of technical indicator descriptions and formal standard operating procedures or documented system descriptions. I was unable to test whether the indicators in the table below were measurable by alternative means.

<b>Performance indicator</b>	<b>Reported achievement</b>
Report on Collection of domestic and Businesses refuse in all formal and informal areas in Grahamstown quarterly	4 Reports on the Cleaning of formal area
Monthly collection of garden refuse in all 45 identified dumping sites in Grahamstown quarterly	Most legal dump sites could not be cleared for the past four months. For this period the only front end loader the municipality has had to replace the bulldozer that was not in working condition.
Completion of construction of Multi Purpose Indoor Sport Centre in ward 7 by June 2017	The contractor is busy with snags due to delay in construction
Construction of (11) High Mast at Mayfield Housing Projects by June 2017	11 High Mast constructed
Payment of Consultant and takeover of the WTW Plant by March 2017	Payment of the outstanding debt
Report on maintenance items completed for reducing water losses annually	1 Report
Report on the number of indigent households per month with access to free basic electricity	4 Reports on the number of indigent people receiving free basic electricity (Minimum of 1107H/H registration to receive FBE)
Report on the number of indigent households per month with access to free basic electricity	4 Reports on the number of indigent people receiving free basic electricity (Minimum of 5484H/H registration to receive FBE)
Report on the number of indigent households with access to water usage	4 Reports on the number of indigent people receiving free access to water. (Minimum of 4869H/Hs to receive water
Report on the number of indigent households with access free water availability	4 Reports on the number of indigent people receiving free access to water availability (Minimum of 4869H/Hs to receive water

Performance indicator	Reported achievement
Report on the number of indigent households with access free water availability sewer availability	4 Reports on the number of indigent people receiving free access to sewer availability (Minimum of 4869H/Hs to receive water
Report on the number of indigent households with access to free refuse removal services	4 Reports on the number of people receiving free refuse removal services
Report on the number of indigent households with access to free rates and taxes	4 Reports on the number of people receiving free removal services access to rates and taxes
Report on 4 RBIIIG Infrastructure development - James Kleynhans Bulk Water - Belmont WWTW - KwaThatha Bulk Sewer - Mayfied WWTW	Only report on James Kleynhans Bulk Water upgrade in Portfolio committees on the 17/11/16(ID 8;17), 15/06/17(ID 8:16)16/03/17(ID8;19) 17/08/17(ID 8:10) Belmont WWTW - KwaThatha Bulk Sewer - Mayfied WWTW has not started..
Report on 1Project by PDoHS Eluxolweni Plumbing Works project	Project has been taken over by ECDC
Report on 3 Project by DWIS - Bucket Eradication Programme	Bucket eradication programme was reported on the portfolio committee on 15/09/17(ID 8:14), 17/11/17(ID 8:15) and closed out report on portfolio committee of 16/03/17(ID:811)
Upgrading 3m of Kwa Nomzamo Internal Road at Riebeeck East	1 KM upgraded
Approval of design and drawings for the Waainek Bulk Water Supply	Approval of design and drawings for the Waainek Bulk Water Supply

#### Performance indicators were not verifiable

37. I was unable to obtain sufficient appropriate audit evidence to validate the existence of systems and processes that enable reliable reporting of actual service delivery against the indicator, as required by the FMPP. This was due to a lack of technical indicator descriptions and formal standard operating procedures. I was unable to validate the existence of systems and processes for the following indicators by alternative means.

Performance indicator	Reported achievement
Report on Collection of domestic and Businesses refuse in all formal and informal areas in Grahamstown quarterly	4 Reports on the Cleaning of formal area
Monthly collection of garden refuse in all 45 identified dumping sites in	Most legal dump sites could not be cleared for the past four months. For this period the only front end loader the



<b>Performance indicator</b>	<b>Reported achievement</b>
Grahamstown quarterly	municipality has had to replace the bulldozer that was not in working condition.
Completion of construction of Multi Purpose Indoor Sport Centre in ward 7 by June 2017	The contractor is busy with snags due to delay in construction
Construction of (11) High Mast at Mayfield Housing Projects by June 2017	11 High Mast constructed
Payment of Consultant and takeover of the WTW Plant by March 2017	Payment of the outstanding debt
Report on maintenance items completed for reducing water losses annually	1 Report
Report on the number of indigent households per month with access to free basic electricity	4 Reports on the number of indigent people receiving free basic electricity (Minimum of 1107H/H registration to receive FBE)
Report on the number of indigent households per month with access to free basic electricity	4 Reports on the number of indigent people receiving free basic electricity (Minimum of 5484H/H registration to receive FBE)
Report on the number of indigent households with access to water usage	4 Reports on the number of indigent people receiving free access to water. (Minimum of 4869H/Hs to receive water
Report on the number of indigent households with access free water availability	4 Reports on the number of indigent people receiving free access to water availability (Minimum of 4869H/Hs to receive water
Report on the number of indigent households with access free water availability sewer availability	4 Reports on the number of indigent people receiving free access to sewer availability (Minimum of 4869H/Hs to receive water
Report on the number of indigent households with access to free refuse removal services	4 Reports on the number of people receiving free refuse removal services
Report on the number of indigent households with access to free rates and taxes	4 Reports on the number of people receiving free removal services access to rates and taxes
Report on 4 RBIIG Infrastructure development James Kleynhans Bulk Water - Belmont WWTW - KwaThatha Bulk Sewer - Mayfied WWTW	Only report on James Kleynhans Bulk Water upgrade in Portfolio committees on the 17/11/16(ID 8;17), 15/06/17(ID 8:16)16/03/17(ID8;19) 17/08/17(ID 8:10) Belmont WWTW - KwaThatha Bulk Sewer - Mayfied WWTW has not started..

<b>Performance indicator</b>	<b>Reported achievement</b>
Report on 1Project by PDoHS Eluxolweni Plumbing Works project	Project has been taken over by ECDC
Report on 3 Project by DWIS - Bucket Eradication Programme	Bucket eradication programme was reported on the portfolio committee on 15/09/17(ID 8:14), 17/11/17(ID 8:15) and closed out report on portfolio committee of 16/03/17(ID:811)
Upgrading 3m of Kwa Nomzamo Internal Road at Riebeeck East	1 KM upgraded
Approval of design and drawings for the Waainek Bulk Water Supply	Approval of design and drawings for the Waainek Bulk Water Supply

## **Reliability**

### **Reported achievement not supported by sufficient appropriate audit evidence**

38. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of 11 targets. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements detailed in the table below.

<b>Performance indicator</b>	<b>Planned Performance</b>	<b>Reported achievement</b>
Report on Collection of domestic and Business refuse in all formal and informal areas in Grahamstown quarterly	4 reports on the cleaning of formal areas	Report were submitted in the following Portfolio Committee SD 14/09/17-SD 8.5- 8/06/17,SD 8.4- 3/08/17(SD8.14),6/06/8.15/17
Payment of Consultant and takeover of the WWTW Plant by March 2017	Payment of outstanding debt	Outstanding payment was processed
Report on maintenance items completed for reducing water annually	1 report	Report are submitted to portfolio quarterly
Report on the number of indigent households per month with access to free basic electricity	4 reports on the number of indigent people receiving free basic electricity (Minimum 1107H/H registration to receive FBE)	4 Reports on the number of indigent people receiving free basic electricity (Minimum of 1107H/H registration to receive FBE)
Report on the number of indigent households	4 Reports on the number of indigent	4 Reports on the number of indigent people receiving free basic electricity

<b>Performance indicator</b>	<b>Planned Performance</b>	<b>Reported achievement</b>
per month with access to free basic electricity	people receiving free basic electricity ( Minimum of 5484H/H registration to receive FBE)	(Minimum of 5484H/H registration to receive FBE)
Report on the number of indigent households with access to water usage	4 Reports on the number of indigent people receiving free access to water. (Minimum of 4869H/Hs to receive water)	4 Reports on the number of indigent people receiving free access to water. (Minimum of 4869H/Hs to receive water)
Report on the number of indigent households with access free water availability	4 Reports on the number of indigent people receiving free access to water availability (Minimum of 4869H/Hs to receive water)	4 Reports on the number of indigent people receiving free access to water availability (Minimum of 4869H/Hs to receive water)
Report on the number of indigent households with access free water availability sewer availability	4 Reports on the number of indigent people receiving free access to sewer availability (Minimum of 4869H/Hs to receive water)	4 Reports on the number of indigent people receiving free access to sewer availability (Minimum of 4869H/Hs to receive water)
Report on the number of indigent households with access to free refuse removal services	4 Reports on the number of people receiving free refuse removal services	4 Reports on the number of people receiving free refuse removal services
Report on the number of indigent households with access to free rates and taxes	4 Reports on the number of people receiving free removal services access to rates and taxes	4 Reports on the number of people receiving free removal services access to rates and taxes
Upgrading 3m of Kwa Nomzamo Internal Road at Riebeeck East	No planned target	1 KM upgraded

## **KPA 2 Local Economic Development**

### **Reliability**

#### **Reported achievement did not agree with the evidence provided**

Report on crafters supported by the municipality to participate in the NAF

39. The reported achievement for the target relating to 4 crafters participated in the NAF projects was misstated as the evidence provided indicated 3 crafters participated in the NAF projects and not 4 Exhibitor funded as reported.

#### **Number of work opportunities created through Municipal Programme**

40. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of target one report submitted to Council. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of one report submitted to Council.

Proof that municipal financial and technical support yielded positive impact in terms of tourism growth and the functioning of Makana Tourism

41. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of target 4 quarterly reports submitted to Portfolio Committee. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of 4 quarterly reports submitted to Portfolio Committee.

### **Other matter**

42. I draw attention to the matter below.

#### **Achievement of planned targets**

43. Refer to the annual performance report on page(s) x to x; x to x for information on the achievement of planned targets for the year and explanations provided for the under / overachievement of a number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 34 to 40 of this report.

## **Report on audit of compliance with legislation**

### **Introduction and scope**

44. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with

specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

45. The material findings on compliance with specific matters in key legislations are as follows:

#### Revenue management

46. An adequate management, accounting and information system which accounts for revenue was not in place, as required by section 64(2) (e) of the MFMA.
47. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
48. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

#### Asset management

49. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
50. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA

#### Expenditure management

51. Money owed by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the Municipal Finance Management Act
52. Effective steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by inadequate composition of the bid adjudication committee and invalid deviations.
53. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R6, 6 million, as disclosed in note 40 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.

#### Liability management

54. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2) (a) of the MFMA.
55. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA

#### Budget management

56. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the unauthorised expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the

disclosed unauthorised expenditure was caused by non-cash items which were not budgeted for.

#### Annual financial statements and annual report

57. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.
58. The annual performance report for the year under review did not include a comparison of the performance with set targets and comparison with the previous financial year, as required by section 46 (1)(b) of the MSA.

#### Strategic planning and performance management

59. KPIs were not set for the provision of basic water, sanitation, electricity and solid waste removal services as required by section 43(2) of the MSA and municipal planning and performance management regulation 10(a).
60. The SDBIP for the year under review did not include monthly revenue projections by source of collection and the monthly operational and capital expenditure by vote as required by section 1 of the MFMA.

#### Procurement and contract management

61. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of by SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
62. Some of the quotations were accepted from prospective providers who were not on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulations 16(b) and 17(b).
63. Some of the quotations were accepted from bidders whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43. Similar non-compliance was also reported in the prior year. Similar non-compliance was also reported in the prior year.
64. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1). Similar non-compliance was also reported in the prior year. .
65. Some of the invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM regulation 22(1) and 22(2). Similar non-compliance was also reported in the prior year. .

66. Competitive bids were not always evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services AND/OR at least one SCM practitioner of the municipality, as required by SCM regulation 28(2). Similar non-compliance was also reported in the prior year. i.
67. Some of the contracts were awarded through a competitive bidding process that was not adjudicated by the bid adjudication committee.
68. Some of the competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). Similar non-compliance was also reported in the prior year.
69. Sufficient appropriate audit evidence could not be obtained that the preference point system was applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework.
70. Some of the contracts were awarded to bidders based on preference points that were not allocated and calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
71. Some of the contracts were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of Preferential Procurement Policy Framework Act and Preferential Procurement Regulations.
72. Bid documentation for procurement of some of the commodities designated for local content and production, did not stipulate the minimum threshold for local production and content as required by Preferential Procurement Regulation 9(1)
73. Commodities designated for local content and production, were procured from suppliers who did not submit a declaration on local production and content as required by Preferential Procurement Regulation 9(1).
74. Commodities designated for local content and production, were procured from suppliers who did not meet the prescribed minimum threshold for local production and content, as required by Preferential Procurement Regulation 9(5).
75. Sufficient appropriate audit evidence could not be obtained that all extensions or modifications to contracts were approved by a properly delegated official, as required by SCM regulation 5. Similar non-compliance was also reported in the prior year.
76. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year. .
77. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, in contravention of section 116(2)(c) of the MFMA. Similar non-compliance was also reported in the prior year.

### Consequence Management

78. Some of the fruitless and wasteful expenditure was certified by council as irrecoverable without having conducted an investigation to determine the recoverability of

the expenditure, in contravention of section 32(2)(b) of the Municipal Finance Management Act

79. Some of the fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the Municipal Finance Management Act .
80. I could not obtain sufficient appropriate evidence that unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the Municipal Finance Management Act.
81. Irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the Municipal Finance Management Act .

#### Other information

82. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the Mayor's foreword and executive summary, the audit committee's report. The other information does not include the financial statements, the auditor's report thereon and those selected development priorities presented in the annual performance report that have been specifically reported on in the auditor's report.
83. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
84. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
85. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate, however, if it is corrected this will not be necessary.

#### Internal control deficiencies

86. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis qualified of opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.



- Leadership has not instituted all the disciplines necessary to enable effective oversight that promotes efficiency and effectiveness in financial management, performance reporting and compliance with legislation. The inability to appoint an accounting officer has contributed to leadership not providing effective oversight over the implementation and monitoring of internal controls. The lack of leadership undermines accountability in the municipality, resulting in the modified audit opinion on the financial statements, performance reporting and material non-compliance with legislation.
- The control environment at the municipality is inadequate, with inadequate daily and monthly processing and reconciliation of transactions. The submitted financial statements contained numerous material misstatements that were not identified by the municipality's deficient system of internal control. In addition, underlying information was not adequate to support all the balances and transactions presented in the financial statements resulting in a modified audit opinion for the year under review. Furthermore, compliance with legislation was not monitored adequately throughout the year, resulting in numerous material findings on compliance with legislation.
- The annual performance report was not supported by complete, relevant and accurate information. Records management was inadequate and not systematically and regularly monitored by management to ensure that information was easily retrievable and available for audit purposes.
- Although an internal audit unit and the audit committee existed during the financial year, their effectiveness was impacted negatively because leadership failed to respond to the recommendations of internal and external audit.

Auditor General

East London

30 November 2017



AUDITOR-GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## **Annexure – Auditor-general’s responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality’s compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the financial statements as described in the auditor’s report, I also:
  - Identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality’s internal control.
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
  - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor’s report. However, future events or conditions may cause a municipality to cease to continue as a going concern.
  - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

### **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

4. I also confirm to the accounting [officer/ authority] that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and here applicable, related safeguards.